SECTION 3: IC INQUIRY

INDUSTRY COMMISSION INQUIRY - TOBACCO GROWING AND MANUFACTURING INDUSTRIES: A SUBMISSION BY PHILIP MORRIS LIMITED

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1. Introduction

Philip Morris makes this submission to the Industry Commission as it prepares to consider the appropriate structures within which the tobacco industry will operate after the termination in 1995 of the Tobacco Industry Stabilisation Plan (TISP) and the Local Leaf Content Scheme (LLCS).

This submission is presented on behalf of Philip Morris Limited, a wholly owned subsidiary of Philip Morris (Australia) Limited. Philip Morris is a unit of the world-wide Philip Morris Group of Companies, one of the world's largest packaged consumers goods companies.

We have endeavoured to answer in details all the matters raised by the Commission in its Terms of Reference and Issues Paper issued in November, 1993. We also provided information to the Commission when it inspected the Philip Morris Moorabbin plant in November.

While not raised by the Commission in the Terms of Reference or the Issues Paper, we have addressed in this submission our concerns at the effect of GATT tariffication on government policy on protection for the tobacco industry.

Finally, we note the Commission is to report to the government within 9 months. While our submission is comprehensive, we look forward to further assisting the Commission at the hearings to be held at a later date.

1.1 Philip Morris Tobacco Company Perspective

Philip Morris Limited, the tobacco manufacturing and marketing company whose major activity is cigarette manufacture, has a primary interest in the development of a viable and internationally competitive Australian tobacco industry in the period after 30 September, 1995 when the Tobacco Industry Stabilisation Plan (TISP) and the Local Leaf Content Scheme (LLCS) will be terminated by the Federal Government.

We have broadly outlined the economic contribution of the combined Philip Morris group.

The Philip Morris tobacco company, as a key component of the group, continues, in its own right, to make an important contribution to the Australian economy.

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Direct, tobacco company contribution in 1993 amounted to $....., of which taxes was $..... and salaries and wages $..... If you extrapolate the flow-on-effect to other businesses and services, the estimated impact is around $..... Over the past five years, the full economic effect, including flow-on, is estimated to be $.....

Figure 4 below, details the economic impact of the tobacco operation in the period 1989 to 1993.

In addition, the tobacco company has achieved export revenues of $..... over the past five years.

Philip Morris believes there is considerable potential for the export of larger quantities of cigarettes from Australia. Conversely, without an increase in exports, coupled with a further decline in cigarette consumption, you could see disinvestment, rather that investment, by the tobacco manufacturers and growers in Australia.

We detail in another part of this submission, the potential for greater export earnings over coming years, given consideration to issues such as quality, price and grading post 1995.

The Philip Morris tobacco company has made a concerted effort over a long period of time, particularly the past two years, to bring the benefits to Australian growers of its US company's agronomic research and development program.

Through the Philip Morris *"Partners in Quality Program"* we have worked with growers with the objective of bringing Australian leaf quality up to international standards.

In addition to the mandated research and development investment through LLCS to the Tobacco Research and Development Council,, which amounts to more than $100,000 annually, a further $50,000 has been invested in Australia by Philip Morris.

The Philip Morris tobacco company is committed to the long-term viability of its Australian manufacturing and marketing operation, while also prepared to continue to work with all parties to ensure a viable tobacco growing industry post-1995.

We believe a viable future for the tobacco industry in Australia rests, to a large extent, with a consistent improvement in the quality of locally grown tobacco leaf as one component of on-going improvements in growing methods, productivity and efficiency gains, and an enhanced international marketing focus by the entire industry post full deregulation.

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Since the last industry inquiry in 1987, there has been little overall change in local leaf quality, however, Philip Morris believes further improvement is vital if Australian leaf is to remain as a competitive input to local cigarette product alongside leaf from other countries.

Phillip Morris' views on the importance of quality improvements are expressed in some detail elsewhere in this submission.

Philip Morris, while committed to the Australian tobacco industry, is of the firm belief that the industry has to have the ability to compete in an international marketplace without the current protection and assistance afforded by TISP and LLCS, provided there is a requisite improvement in quality accompanied by improved agriculture effectiveness.

Post 1995, with the termination of TISP and LLCS, Philip Morris will look to Australian growers to lift quality standards consistently and, with new industry marketing and selling arrangements in place, the opportunity exists for a potentially viable future for growers on a price competitive basis. Broadly, Philip Morris does not support continued protection of tobacco growers, but wants growers to be valued suppliers to manufacturers on an internationally commercial basis.

Additionally, Philip Morris sees no benefit in phasing down tariff protection, but is firmly of the opinion that a quick change to an open market will most efficiently facilitate the necessary changes. The termination of TISP will bring about the more open and free market, and withdrawal of the LLCS will give the necessary impetus for leaf quality improvements.

Philip Morris has a long-term commitment to the Australian market, provided leaf is quality and price competitive, and supply is consistent.

2. Market Trends

The Commission invites advice on perceptions of emerging trends in the domestic and global markets for tobacco and tobacco products, the factors which influence production, consumption and trade flows, and likely future developments.

2.1 Leaf production

Current worldwide tobacco leaf production is estimated at 7.3 billion kilos (reference USDA statistics for 1992).

Major producers are identified in *(Appendix, Fig. 4)*, with associated consumption data and leaf stocks in *(Appendix, Fig. 5)*.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Detailed information on total tobacco and flue-cured tobacco production can be found in *(Appendix, Fig. 6 and 7)*. Specific details of volume, areas and farm values for the years 1987/1991 are in *(Appendix, Fig. 8)*.

The farm-gate value of worldwide leaf production is difficult to ascertain because of exchange rate movements and reported statistics are not always reliable. However, the following estimates (USDA 1993) show farm-gate values, and volumes, for leaf (of all types) produced by some countries in 1993:

Producer	Volume (kilos)	Farm-Gate Value ($US green/kg)
China	3.3 billion	60-70c
USA	660 million	3.65
Brazil	509 million	1.22
India	518 million	1.00
Zimbabwe	201 million	1.35

In 1993, Australia's leaf crop produced 12.5m kilos at an estimated farm-gate value of $A6.14 ($US4.175 @ 0.68) per kg. In 1994, 8.1m kgs at an estimated $A6.03kg ($US4.10).

2.3 Leaf consumption

The major tobacco leaf consuming countries are China, India, the United States, India, the countries of the European Common Market (EEC), Japan, Brazil and Indonesia. Large volumes of leaf are used by some countries, although they are not necessarily heavily involved in world trade of the leaf because they grow domestically for their own use.

The major international exporters of tobacco leaf are Brazil, USA, Zimbabwe, Greece, Malawi, Turkey and Italy.

Brazil, the USA and Zimbabwe are the main exporters of flue cured tobacco. The countries of the EEC are major leaf consumers, buying all types of tobacco (flue cured, burley and oriental) worldwide from all major trading countries. The USA, the Russian Federation, Japan, European Free Trade Association, Egypt and China are all important importers. Egypt is a major importer, the former Communist Bloc takes some leaf and China smaller volumes.

2.4 Tobacco Products Consumption

Appendix *Fig. 9* shows cigarette production in selected countries, including products consumed both domestically and exported, whilst

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Fig. 10 details cigarette export and import figures. *Fig. 11* identifies cigarette production trends in specific countries.

The consumption of made up tobacco products (primarily cigarettes), in general terms, has declined in the major western countries, including North America, Europe and Australia.

In the rest of the world, generally classified as the underdeveloped countries (i.e. China, India and Indonesia) consumption has grown as per capita wealth has increased, with the greater usage of machine-made cigarettes, rather than hand-made or locally made products. There has been an accompanying decline in the nicotine and tar delivery due to the greater degree of technology and manufacturing consistency applied by international manufacturers.

Consumption has declined noticeably as a result of fiscal policies in some countries (e.g. Brazil), but the general trend is upwards.

In developed Asian countries (i.e. Japan, Singapore) there has also been a general increase in the consumption of tobacco products, although not as marked an increase as in the under-developed countries.

The increased domestic consumption trends in developing countries have, in general, been in the order of 1 to 1.5%. Decreased consumption levels in Western nations are 2% in the US, 1 to 1.5% in Europe.

In Australia, tobacco products consumption has declined by 10 to 12%. (CHART REQUIRED)

International trends forecast a continuing, modest increase in world consumption of tobacco over the next 5 to 10 years. However, while overall world consumption may increase, particularly in developing countries, offsetting may occur in specific countries due to taxation and health-related measures.

As the former Communist Bloc countries and underdeveloped nations gain increasing wealth, and disposable incomes rise, they have the potential to absorb many more tobacco products than currently consumed, particularly machine manufactured cigarettes of international specifications.

Consumption is expected to grow in the Asia-Pacific countries, although there may be tax and health-related pressures. Consumption in China, especially, is expected to grow as the market opens up. Indonesia, with increasing wealth, is expected to move away from

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Kretek and locally made products to international-style, machine-made cigarettes.

As international companies progressively trade in new and expanding markets, there will be pressure on local tobacco and tobacco products manufacturers to move to international product standards.

The relaxation of tariff and other barriers is expected to result in increased trade opportunities for international cigarette brands in the Asia-Pacific, with regional growth in consumption around 2% annually.

2.5 Future Leaf Supply/Demands

International trends in demand for tobacco leaf (not made up products) in 1993 saw supply exceeding demand, a situation likely to continue in 1994-95, and possibly 1996. This would drive leaf production significantly down in the major producing countries such as the US, Brazil and Zimbabwe.

A reduction in supply and a move towards supply/demand balance is expected in 1996.

The underlying international usage trend, however, is still around 6.5 billion kilos for raw tobacco. Modest increases are forecast to 1997 and beyond.

In Australia (given that manufacturers maintain usage at around 57%) demand for all leaf is expected to decline at between 2 and 5% over the next 3 to 4 years, bringing domestic leaf usage to around 9.5 and 10.5 million kgs dry weight per annum from the current (INSERT NUMBER) kgs..

Imports will follow a similar overall trend, but the proportion used could be significantly impacted by developments in the domestic leaf producing industry.

3. Structure and Competitiveness

The Commission seeks to examine the current structure and competitiveness of the industries, drawing international comparisons where appropriate. Requests include:

- *What influence has the existing assistance and adjustment arrangements had on the structure of these industries?*

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- *How does Australian tobacco growing compare internationally, with respect to price, input costs, farm size, and quality of tobacco grades?*
- *How do Australian tobacco products compare internationally in terms of price, input costs, quality of product?*
- *Why are some products imported, while others are exported from Australia?*
- *What characteristics differentiate the imports and exports and make them competitive in their respective markets?*

3.1 Leaf Production, Quality, Prices, International Competitiveness

The current stabilisation program, through the local user scheme, has effectively provided growers with tariff protection. Australian manufacturers are encouraged, through the duty system, to use above a certain level of domestic tobacco.

Local growers enjoy a stronger price negotiating position because manufacturers pay less duty on imported tobacco if they use a certain proportion of domestic. However, while manufacturers effectively have some incentive to use domestic tobacco, there is a negative effect on local growers who are less world competitive on price and quality.

The base duty level on imported tobacco is about $A1.42 cents per kilo. However, because of the price offset for greater use of domestic tobacco, (currently 57%) the effective rate of duty on imported tobacco averages approximately 25 cents a kilo for leaf from recognised developing countries.

Manufacturers would have a greater incentive to use a higher percentage of Australian tobacco if quality was comparable to competing international product, and local tobacco was competitive with world prices. The ability to select only the required grades, and to operate as freely in the domestic market as in the international market, would also be a significant influence.

International leaf prices declined significantly in 1992 and 1993 while Australian prices remained high. With world prices expected to decline yet again in 1994, Australian prices will be significantly overpriced in 1994 and 1995.

Australian growers have a major challenge, particularly in the post-1995 deregulation period, when their current average quality of

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tobacco leaf could be overpriced, in world terms, by as much as 25 to 30%.

Fig. 12 (insert source) indicates the movement of the industry submitted import distribution price movements between 1990 and 1993, realised average prices for Australian tobaccos and projections to 1996.

This indicates a low ISP target for growers to achieve by 1996. To insulate both manufacturers and growers against movements in world prices, we believe it would be appropriate to take an average, for the period 1990/1993 inclusive, of 453.1 cents per kilo.

With quality improvement, growers have the potential to improve returns above this level, perhaps to $A5.00 per kilo.

Improvements in quality, productivity, efficiency, production costs and crop management generally would assist in overcoming the price disadvantages of Australian growers.

Industry inventory and adjustment costs (not changes in the base usage level) agreed under the stabilisation program, mean that production volumes of the Australian crop will decline from 12.5 million kilos in 1993 to 8.1 million kilos in 1994, potentially remaining depressed in 1995, with foreseen *"recovery"* to usage levels until 1996.

The industry has agreed an inventory target by 1 January 1996 equivalent to 10 months of projected use.

In reality, the base usage rate in 1994 is likely to be something in excess of 10 million kilos dry weight and, even though the market may continue to shrink into 1995, base usage should remain close to 10 million kilos dry weight.

For 1996, we foresee a situation where base usage, provided all manufacturers continue to use 57%, could be around 9.7 to 9.8 million kilos.

From a manufacturer's perspective, the industry will be driven by the competitive position of the Australian growers, with quality versus price a key determinant.

Quality is absolutely critical. If there was a dramatic improvement in the quality of Australian leaf, Philip Morris envisages a much higher probability of manufacturers maintaining, or increasing, domestic tobacco purchases.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Conversely, if quality does not improve significantly, or indeed deteriorates, it is unlikely domestic tobacco will be competitive. There would then be pressure on manufacturers to question the continued use of 57% domestic leaf in an unprotected environment. If quality does not improve, there is every potential that domestic leaf usage will decline, especially if it is not price competitive.

Fig. 13 (INSERT SOURCE) shows selected historical data comparing prices and production levels of major flue cured tobacco categories and countries.

The Commission will be aware that Australian growers currently produce what has been commonly referred to as filler tobacco at the lower end of the quality scale. The highest quality classification is fully aromatic, currently only produced in the US. The middle quality classification is semi-aromatic, of which Brazil, Zimbabwe and Malawi are the major producers.

The potential for Australian growers to be competitive is significantly diminished if they continue to produce tobaccos in the lower priced, filler end of the market.

The best interests of Australian growers lie with raising quality to the semi-aromatic sector where the prices for the product are higher. Current international prices for filler return to growers somewhere between 50 and 60 cents ($US) a kilo at farm gate, or even less. Australian growers cannot produce to meet a sale price of 50 to 60 cents.

However, if you look at the quality markets - say the semi-aromatic classification - growers trading internationally are receiving $US2.50 ($A3.68) to $3.00 ($A$.40) green. Given our current level of farm input costs, the potential for Australian growers to compete internationally is enhanced if they produce a higher quality with returns equivalent to these levels, and allowing for import substitution cost consideration.

This is a reasonable and achievable objective, but only if there is a total revamp of cultural practices, with greater emphasis on quality rather than the current emphasis on yield. Input and production costs will also have to be closely controlled.

There will be potential to open up international markets for Australian produced leaf if quality is moved to the semi-aromatic level. While it would be a tough competitive environment in which to

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operate, that is an objective that all manufacturers, and the good growers, would like to achieve.

When making international leaf comparisons, it is important to note that Australian tobacco delivers its own taste profile. With the removal of the Local Leaf Content Scheme, and if Australian manufacturers moved to less than 57% domestic leaf usage, the distinctive taste profile would probably dictate a phase-out period, perhaps over two to three years, rather than a sudden change to other leaf sources.

Traditionally, all manufacturers are very cautious in introducing changes to their products which can result in negative consumer reaction.

However, if manufacturers continue Australian leaf usage at all, it has to be approximately 50% to be commercially viable. If content drops significantly below 50% the industry would progressively wind-back below the critical mass required to support the processing and marketing infrastructures. Therefore, quality improvement remains the key issue.

Australian leaf quality is also adversely affected by its imbalance of chemical constituents. (*Fig. 14*) and the lamina/stem ratio of leaf produced. (See charts in *Fig. 15* and *16*).

If leaf quality improves there is the potential for usage in excess of 57% content in the longer-term, although probably not on a run-of-crop basis, but with manufacturers detailing preferred grades. Trading terms would need to also reflect the world situation.

3.2 Local Tobacco Products International Competitiveness, Quality

Current domestic cigarette manufacture accounts for approximately 98% of locally consumed products. Only an extremely small proportion of imported product is consumed.

Of the total Australian cigarette market of 30 plus billion sticks annually, only approximately 1.9%, or about 600 million, are imported product. (CONFIRM FIGURES WITH PLANNING/MARKETING).

Imports are primarily at the extreme luxury end of the market with very specialist taste profiles. Hand-rolled products, pipe tobacco and cigars have a significantly higher share of imported product. (HERE WE NUMBER)

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

If Australia is to compete in the global, manufactured cigarette market, or even just regionally in the Asia-Pacific market, taste profile is of major importance.

If significant proportions of Australian tobacco as currently produced, are used, we would expect problems. Australian tobacco does not have the taste profile, or even the chemical performance, to allow it to be competitive with other internationally produced Virginia cigarettes now sold in the Asian market.

If quality improves, the situation could potentially change, with Australian tobacco more readily used in export products manufactured in Australia.

Cigarettes are currently exported from Australia using a significant proportion of Australian leaf, but sales volumes are extremely small. However, the balance of trade on manufactured product is now in Australia's favour by about 3 to 1, with nett exports currently in excess of imports at around (NEED FIGURES) .....sticks exported annually.

4. Exports

The Commission requires information on the extent of exports of Australian leaf and tobacco products, the countries which constitute the major markets for exports, and the competitors in those markets.

In addition, the Commission asks if different health standards or labelling requirements in different countries affect exports and, if so, how?; what costs are involved in producing different labelling for the exported, manufactured tobacco product?; there was a recent example of one manufacturer exporting tobacco leaf, after treating it with its own specially developed technology. Could this treatment be used more extensively to make Australian tobacco leaf more attractive to overseas buyers, or was this a 'one-off' sale?

The Commission is asked to report on the potential for further development of the industries, including the scope for increasing exports while, at the same time, taking account of Australia's international approach in relation to tobacco and health?

What are the barriers to the export of tobacco leaf and tobacco products?; subject to Australia's international approach in relation to tobacco and health, what is the scope for further developing the industries, including increasing exports of both leaf and manufactured products and given that the TISP and LLCS will terminate in September 1995?; is Australia's international approach to health and tobacco a barrier to export development?

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

4.1 Leaf Export Levels, Potential Markets

There have been very limited exports of Australian leaf. The 250 tonnes purchased from Australian growers in 1993 was largely to satisfy a one-off sale by Philip Morris of semi-processed product to one Asian country.

There is only limited potential for leaf exports in the true filler market, the category currently produced in Australia. Other lower priced countries readily undercut Australia in the international filler leaf market, and will continue to do so due to significantly lower production costs.

The mid-level, semi-aromatic market is the level for Australia to compete in. A commitment to consistent quality upgrading across the Australian crop is required, and even then sales potential may not be realised in this very competitive market. Leaf purchasing decisions would be made on a strict commercial basis, with consideration of tobacco requirements including smoking quality, chemical constituents and long-term supply of paramount importance.

Philip Morris' own international leaf buyers in the US and Europe have previously commented unfavourably on Australian standard leaf grades. On both a quality and value/price basis Australian leaf was nowhere near competitive.

4.2 Health Standards/Labelling Standards for Exports

If the quality standards are met, we would not expect the health standards and labelling requirements in other countries to be a major issue affecting entry of those products into export markets, although manufacturers could incur higher manufacturing costs per pack to meet labelling specification for different countries.

However, if Australian growers continue to produce tobacco with relatively high nicotine content that could exclude them from potential sales in specific markets. To correct the problem, local growers have to use less nitrogen, grow crops faster and grow in the right season. In short, growers need to acquire a greater level of market awareness and understanding of the end-users of their product.

4.3 Special Export Treatment

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

The special treatment in 1993 of an export shipment of tobacco leaf was a one-off deal by Philip Morris (this information is *confidential* to Philip Morris) and does not represent any ongoing opportunity to build further export business by utilisation of this method.

4.4 Barriers to Tobacco Leaf and Tobacco Products Exports

Australian leaf quality and price are still the main barriers to competing internationally, as outlined in some detail. The other potential barrier, is the lack of international marketing expertise amongst Australian growers.

Australian Growers need to become more market focussed to succeed in selling leaf in international markets, where they would be competing with highly qualified international dealers. Growers would be best advised to have those established dealers act on their behalf on a commission basis.

4.5 Trade Marks

(INFORMATION FROM LEGAL)

5. Factors Affecting Efficiency and Structure/Arrangements Affecting Supply

The Commission invites comment on how the removal of the local content and stabilisation plans and related programs will impact on individual participants in the industry. Elements of the assistance schemes where there may have been impact include marketing quotas; limitations on the transfer of quota; leaf and grade price schedules; allocation rather than competitive bidding for leaf; export assistance; funding of research and development; subsidised irrigation water in some areas.

The Commission suggested that since the inception of TISP and the LLCS, modifications have been made in order to encourage greater efficiency and to gradually reduce the level of assistance to the tobacco growing industry - ie barriers to quota transfers have been virtually eliminated; attempts have been made to reduce the size of manufacturers' leaf stockholdings; prices for leaf have been set to gradually bring them closer to the import parity price.

5.1 Marketing Quota System

With the inter and intra state transfer system broken down, the marketing quota system is much freer. Unfortunately, farmers are still growing tobacco which is not necessarily of the quality demanded by the market. Whilst these growers may still be viable as a very

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

small unit, they may not be viable in international terms on price and/or quality, most specifically quality.

5·2 Leaf and Grade Price Schedule

The leaf and grade price schedule has had a negative impact on the industry by not, in effect, rewarding those areas that reflect manufacturers' demands, for example:

- Few price levels have resulted in "insensitivity" (price gaps too wide)
- Emphasis on colour has been misleading
- Grade/price structure has rewarded production of tonnes/hectares, not quality
- No recognition, or delayed recognition, of the importance of maturity/texture/oiliness of leaf
- Grower refusal to accept change, reinforced by TISP/LLCS
- Research effort (especially North Qld) has focused on exploiting grade/price schedules, with no attempt to reflect buyer interests

The industry arbitration procedures are totally negative, serving only to create conflict between growers and buyers and, most important, protecting poor growers and not rewarding good growers.

The current system is a legacy of history, with undue emphasis on leaf colour, and insufficient emphasis on maturity, ripeness and texture of tobacco.

There is industry agreement to introduce an international classification system for the 1994 and 1995 crops, to run in parallel with the current system, and to form the foundation for the post-deregulation environment. We are concerned this is only a two-year time frame for growers to become comfortable with the new system. In addition, no pricing has yet been established against the new grading system.

While the new, international classification system will introduce an emphasis on leaf maturity, ripeness and texture, we suspect that in 1994, and perhaps even 1995, pricing will still be based on the old grading system.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Agreement has been reached for the price schedule to expand to 24 groups in 1994, with a review post-season 1994. The proposed move to individual grade pricing, post deregulation, is essential if growers are to receive the correct market signals.

Pricing should also be related to the new international classification system as rapidly as possible, preferably before deregulation.

However, if growers are to change attitudes, pricing must reward production of styles required by manufacturers, and penalise where necessary.

5.3 Allocation Versus Competitive Bidding

The Commission seeks comment on allocation rather than competitive bidding for leaf.

The industry has examined a range of alternative marketing systems:

- National Australian Growers entity, trading with manufacturers either as one body or individually
- State grower entities, trading as one
- Open auctions
- Direct contract negotiation between each manufacturer separately, and with individuals/grower groups

Philip Morris has no specific preference for any one option. However, a system of direct negotiation by each manufacturer is likely to be the least efficient and least cost-effective. The company is prepared to participate in any system which is legal, equitable and maintains continuity of supply of a quality product at a commercially competitive price.

On the question of allocation versus competitive bidding, Philip Morris recognises that the latter allows an element of selectivity, and affords any given buyer the opportunity to reward leaf favoured for purchase. However, with only three buyers at auction, there may be insufficient competition to sustain a true auction system.

Allocation does ensure equity amongst all buyers. However, there may be problems if buyers do not distribute their off-take on a pro-rata basis between States, even though this may reflect buyer preferences.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

5.4 Export Assistance/R&D

In terms of export assistance, the key area of focus has been funding of research and development, with government contributing half a percent of the gross value of product (green leaf).

Growers and manufacturers have made an equal contribution to R&D, equivalent, in total, to 5.4 cents a kilo.

Research and development funding will effectively decrease in coming years because of lower volumes and revenues. Measures to deal with the decreases in funding and research are being handled by the Tobacco Research and Development Council (TRDC), of which a Philip Morris employee is a member. The TRDC is considering ways, whereby the decreased funds can be best spent to assist in quality improvement and reduced leaf production costs.

Philip Morris, on its own initiative, has provided company funds for promoting research and development in the growing area, over-and-above the required contribution under the current assistance scheme.

Philip Morris has invested approximately $115,000 in 1993 and a projected $80,000 (1994 ??) as the company's mandatory 2.7 cents per kilo contribution. In addition, the company has contributed in excess of $50,000 through its own program.

There have been three visits in the past two years to Australia of Philip Morris US experts on growing and technology. Philip Morris hosted Victorian, Queensland and New South Wales growers on visits to the US in 1992 and 1993 to study growing methods and the application of the latest technology.

Philip Morris leaf experts at the Moorabbin plant in Victoria have continued to reinforce with local growers, the lessons learnt from the US visits.

Philip Morris' own initiatives have been quite successful in fuelling the process of change, particularly in Victoria, and to a lesser extent in Queensland and New South Wales.

Philip Morris will allocate further funds in 1994 to host additional US study visits by Australian growers, and to ensure the continued transfer of the latest techniques and technologies.

The Philip Morris initiative is complementary to the work of the TRDC.

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Philip Morris believes that a maintenance of current levels of R&D budgets through the TRDC will start to bring a flow-through of benefits to the industry.

5.5 Subsidised Irrigation Water

Water supply for irrigation purposes in the tobacco growing areas is plentiful. However, pricing by local authorities is not facilitating growers to a better competitive position in world markets. This is an issue for negotiation between growers and local water authorities.

6. Tobacco Growing

The Commission invites comment on the effects that the latest TISP and LLCS have had on production, quality of leaf and prices.

- *How have growers been affected by recent changes : ability to sell quotas throughout the country; attempts to reduce the size of the stockholdings; movement towards import price parity and reduction in the aggregate quota?*

Other questions posed by the Commission, include:

- *Has the experience of growers with these changes been a guide to further adjustment in the future?*
- *What role did changes to the local content and stabilisation plans play in reducing the gap between Australia and international prices for tobacco leaf?*
- *Does the administered grade and pricing system cause the prices received for the various grades to differ from those which would be realised in a more open market environment?*
- *Has the quality of Australian leaf improved and, if so, why has this occurred?*
- *As a consequence of the trade of quotas, how has the volume and value of production changed between regions?*
- *What are the reasons for this change?*
- *Are there other changes which have impacted on growers?*
- *When tobacco manufacturing receives tariff-only assistance, what will be the implications for domestic growers?*

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- *How will growers determine how much they will grow?*
- *Is there likely to be a further shift from one growing area to another?*

6.1 TISP Affects

There has been a negative, long-term impact on the leaf growing industry from the protection afforded growers through TISP.

TISP has not served to improve the quality of Australian tobacco, and prices, which in an indexed form, have gone down over time since the system was introduced, are still not internationally competitive.

Generally, tobacco quality has not improved because, through TISP, the incentive has been to improve yields instead of quality.

However, as the industry moves into a deregulated market, there will be more incentive to improve quality.

Without quality improvements, Philip Morris believes manufacturers will progressively use less Australian tobacco.

In a more open market environment, the current administered grade and pricing system is not going to assist the change process. If the new, international system is embraced by the industry it has the potential to assist growers move to a competitive, world market position. Growers' own costs of production, the farm-input costs, is still an issue for them, but, as a market incentive, the new system would be far more reflective of the world market.

6.2 Quotas, Tariff Protection

Trade in quotas has mainly been north from South Queensland and New South Wales to North Queensland. The transfers have primarily been driven by the structure of the old grade and price schedule, bringing with it the problems highlighted elsewhere in this submission. The decline in South Queensland has largely been driven by local economic and infrastructure changes. ***Figure 17*** details quota movements for the period 1978 to 1992.

Broadly, the move of quotas from New South Wales has been correct as quality of tobaccos from this area is generally inferior, and not world competitive. There is no long-term, viable future for tobacco production in NSW.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

The moves from South Queensland to North Queensland appeared logical (CHECK WHEN, WHY OCCURRED ??) at the time. However, as more and more tobaccos are grown in the tropical winter of North Queensland, with inferior smoking quality, we question if these moves have been as beneficial as they first appeared.

The tariff levels after 1995 will be key to the international competitive position of Australian tobacco growers. Lower tariff levels means Australian growers will have to be far more competitive on quality - a desirable outcome for Philip Morris, and consumers.

If growers continue to benefit from tariff protection it will be important for manufacturers to have a similar level of protection applied to imported manufactured products. Without this balanced protection, the sale of imported products containing no Australian leaf could expand to the detriment of both Australian growers and manufacturers, their employees and businesses serving the industry.

6.3 Marketing Systems

The industry has important decisions to make on the marketing systems which should operate in a deregulated market. Philip Morris believes radical change will occur as the industry is restructured and different arrangements are established between growers and manufacturers.

In a free market environment, it is likely that manufacturers nationally would table their leaf needs. It would be up to the growers, negotiating between themselves, to decide who gets what.

Eventually, a situation is envisaged where a manufacturer may choose, at any time, to buy tobacco from one state and not another. That would be a radical change in the industry, but entirely consistent with the government's stated objective of a deregulated, fully competitive industry.

With this outcome, consideration would need to be given to a phase-down period, or an immediate change in 1996.

We believe growers, subject to the requirements of the Trade Practices Commission, are keen to maintain many of the current mechanisms in the marketing system, with as little change as possible.

Philip Morris is seeking only to buy tobacco at the right price and quality level through an efficient marketing system. The alternative systems are, as already indicated, via national or state trading entities dealing with manufacturers, an auction system, or contract growing

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

where manufacturers have direct contracts with individual farmers or co-operatives.

With a system of co-operatives, a situation is envisaged where a manufacturer may choose to deal with, say 65 growers, all of whom may be in Victoria or Queensland. This would prejudice other growers.

Manufacturers' decisions on which growers to deal with would have to be made on the basis of the price and quality of a particular crop resulting in a highly competitive, internationally aligned market. Prices would be pulled down. Quality would go up.

A market operating this way would have no standard pricing nationally, or on a State basis. Instead, separate pricing systems would operate between manufacturer and grower, based on the manufacturer's own crop value assessments.

The areas growing the best tobacco at the same price as the world market would clearly have a better opportunity for sales under this system.

6.4 Grower Production Costs

The basic cost of tobacco production in Australia is a fundamental issue to be addressed. Given tobacco quality can be raised to that of other producing countries, such as Brazil and Zimbabwe, Australian growers would still be disadvantaged because of lower production costs in these other countries.

In addition, the exchange rates in these countries are manipulated to some extent, to keep local industry competitive in many products, including tobacco. However, those countries are only able to sell their tobacco for a certain value, so their conversion costs are not necessarily below Australia.

A key, potential cost reduction for Australian growers is a lower use of fertilisers, especially nitrogen. This would benefit leaf quality and chemistry.

A shortening of the growing period and time in the field should also reduce costs for chemicals (i.e. insecticides and herbicides) as well as reducing management costs. Quality would also benefit, and with curing costs potentially reduced through faster curing, energy costs would come down.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Improved techniques should be further considered, with assistance through the research and development mechanisms to study the good techniques used in countries like the United States.

7. Tobacco Manufacturing

The Commission seeks information on how tobacco manufacturers have responded to the most recent TISP and LLCS.

- *Does the administered price scheme distort production decisions?*
- *Does the selling system result in either lower quality leaf or a less than optimal mix of grade and type of leaf?*
- *How important are price and quality of local leaf in domestic manufacturers' decisions to use local leaf?*

Other recent changes for tobacco manufacturing include the decline in local demand for tobacco products and increases in excise taxes.

- *What are the main reasons why demand for tobacco products has declined?*
- *To what extent is the decline in demand due to government intervention?*
- *After termination of the TISP and LLCS, will manufacturers be able to selectively purchase leaf and generally have more control over their mix of quality and type of leaf?*
- *Although, in terms of months of usage, the stockholding of manufacturers has not been reduced, will this be achieved in the future?*
- *If not, what circumstances might prevent it?*
- *What level of stockholding would be observed in the absence of any agreement/requirement to hold a minimum level?*

7.1 Manufacturer Responses

In response to TISP and LLCS, Philip Morris and other manufacturers have tried to introduce a process of change through the entire system, so that, with deregulation and the right pricing systems in place, growers will know what quantity and quality crops to grow, and how they will be rewarded according to an assessment system, as outlined elsewhere.

7.2 Production Distortions

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

The administered price scheme distorts production decisions because the pricing mechanisms have not reflected real demand on the world market, where focus on quality is paramount.

This means, to some extent, that manufacturers have not had sufficient flexibility to manage their blends because a major component (57%) is basically the same.

7.3 Selling System Affects on Leaf Quality

As stated previously, the selling and pricing systems have not sent the correct signals to growers about the quality of leaf required.

7.4 Manufacturing Decisions on Leaf Usage

Through TISP and LLCS, there is currently an incentive for manufacturers to use local leaf. However, without TISP and LLCS and a free market operating, price and quality, will be absolutely dominant in manufacturers' decision-making on local leaf usage, subject to tariff levels.

A situation will occur where the actual usage and content of Australian domestic leaf may vary up and down, depending on the year, and other factors.

However, it is important to reiterate that manufacturers are reluctant to dramatically change their blends in a short time frame because of issues such as taste profiles. But, while manufacturers would not want to introduce change in tobacco content too quickly, change could, nevertheless, be introduced far more quickly than is perhaps appreciated.

7.5 Decline in Product Demand, Tax Increases

During the 10 years prior to 1991, consumption of cigarettes in Australia had been growing, in absolute terms, at a rate of ___% (CHECK PLANNING FOR NUMBER - Bruce Beardmore).

Since 1991, some decline in consumption has been apparent, almost entirely attributed to the economic conditions prevailing in Australia.

The compounding affects of the reduction of disposable income during the recession, and significant increases of ___% (CHECK NUMBER) in taxation, have driven this volume reduction.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Specifically, price rises cause low outcomes. The "shock" of price rises result in short-term volume declines, which later bounce back to reveal the more underlying decline rate, which is not significant.

Therefore, the effect tax increases have on consumption is somewhat dependant on prevailing economic conditions.

(BRUCE BEARDMORE TO PROVIDE TABLES/CHARTS ETC ON PED???? TO BACK UP QUALITATIVE STATEMENT)

7.6 Selectivity of Leaf Purchase

There will be no change, at this stage, in the selectivity of leaf purchase, with broad industry agreement currently on purchasing run of crop. However, the situation, may change, depending on what marketing models finally emerge with deregulation. With improved quality, the market will be better able to compete and survive. There is the potential for import substitution if prices are competitive.

7.7 Inventory

Philip Morris' tobacco stockholdings are currently well over the agreed industry target of 10 months stock by 1 January 1996. We have not progressed as rapidly as expected in reducing stockholdings, although steps are being taken to correct the previous oversupply position. The crop production levels envisaged for 1994 will continue to address this issue.

To further reduce stockholdings, manufacturers should be free to indicate their requirements without the application of an industry-wide formula, as is the case now. Manufacturers can then manage inventories as they wish. Although this could mean some greater volatility in demand, we believe manufacturers would be willing to give demand indications for, say, a three year horizon. Growers would then have the opportunity to plan investment and production, and make adjustments as appropriate.

8. Policies Affecting Tobacco Consumption (Production/Industry Efficiency Related)

The Commission comments that, while policies affecting consumption can, in general, be considered separately from assistance to production, some may have an impact on the efficiency and performance of the industries. An example of such a policy is the agreement by Federal and State Health Ministers, at a meeting in July of this year, to implement new labelling requirements which will result in warnings occupying 25 per cent of the front of a packet of cigarettes.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

What effect, if any, will these particular changes have on manufacturing costs and on demand?; do differences in State licence fees impact, in any way, on production decisions. If so, how?

How much of the manufacturers' tobacco needs are expected to be sourced locally after the removal of the local content scheme?; are there advantages to manufacturers from using local leaf that offset any price disadvantages. If so, what are these?

8.1 New Labelling Affects on Production

(NEED INFO. ON LABELLING AFFECTS ON PRODUCTION)

8.2 Sourcing Local Leaf

The level of local leaf used will depend on quality, prices and consumer preferences. The advantages of use of local leaf are, potentially, consistency of supply, lower inventory levels than for imported tobaccos (shorter delay in shipping finished product), reduced exposure to fluctuations in exchange rates, and the ability to influence more directly the types of leaf produced.

8.3 State License Fees

(NEED INFO. ON SLF)

9. Arrangements Between Growers and Manufacturers

If the market was completely deregulated, how would the growers and manufacturers respond?; would agreements as to the type and quality of leaf, and their prices, be made between growers and manufacturers. If so, what form would these agreements take?

Now the government has decided to discontinue the TISP and LLCS, the setting of the minimum price and grade schedule and conditions attached to sale should no longer apply. Will this be so, or are alternative arrangements envisaged.

What alternative selling arrangements would growers want to put in place. Would they need approval of the Trade Practices Commission?

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

What role are the State Tobacco Leaf Marketing Boards expected to have after 1995?; how are the powers of the State Boards and their position with regard to the Trade Practices Act likely to change after 1995?

9.1. Selling Schemes/TPC and State Board Roles

The options for alternative selling schemes and arrangements between manufacturers and growers have substantially been answered in *Section 5.1.3* and *5.1.4*. (CHECK REFERENCE IS CORRECT)

We acknowledge the Trade Practices Commission has laid emphasis on ensuring that competition be maintained in the growing and manufacturing sectors, and that the quota system of production be deregulated.

We see no particular role for State Boards post deregulation, given introduction of a market-driven structure.

10. Policies Affecting Consumption (Consumer, Taxation, Social Costs Related, etc)

The Commission states it is required to take account of the economic, social, health and environmental objectives of governments. The following policies are primarily directed at health and public safety concerns associated with tobacco products:

- *prohibitions on smoking in certain locations*
- *prohibitions on the sale of tobacco to minors*
- *prohibitions on advertising*
- *segregation of smokers from non-smokers*
- *labelling requirements for specific health warnings*
- *publicly funded anti-smoking campaigns*
- *child education programs, and*
- *voluntary limit put on tar, nicotine and carbon monoxide content, developed in agreement with the department of health*

The Commission asks, what effects have the health and public safety interventions had on the consumption of tobacco products in aggregate?; are measures, such as bans on smoking in particular locations, more effective than taxation in dealing with problems such as passive smoking?

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Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

It is in the consumption area that claims are made that market outcomes need correcting. Arguments put forward to justify government intervention include that smoking is an environmental carcinogen, that nicotine is a toxin, and that teenagers are too young and impressionable to make decisions about smoking which are in their long-term best interest. Much of the government intervention on the consumption side is justified on the grounds of trying to correct for the negative effects that tobacco has, or is perceived to have, on health.

In addressing the question of Federal and State Government objectives with respect to tobacco and health, the Commission notes that Ministers of these governments, through the MCDS (Ministerial Council on Drug Strategy) unanimously agreed on the need for clearer, stronger warnings to discourage people from smoking , and especially to stop children taking it up.

The Commission asks: Does this adequately reflect the attitudes of all governments to smoking, or is it more complex than this?; participants may wish to comment on the reasons why they think that market outcomes are not desirable and could be improved with government intervention; are the current policies and programs designed to effect consumption the most effective means of achieving the health and other objectives of governments, or could improvements be made?

With respect to health, the Commission has been asked to take account of Australia's international approach to tobacco and health. Australia's international position is relevant to the export potential of the industries and has a direct effect on production, rather than consumption, within Australia.

10.1 Passive Smoking (ETS), Workplace, Public Place Restrictions

The Commission poses the premise that Environmental Tobacco Smoke (ETS), often referred to as "passive smoking", is a proven health risk, a position which Philip Morris rejects, and which is not supported by a body of scientific and other evidence internationally.

Passive smoking is a far more complex issue than state and federal governments, and their instrumentalities, have acknowledged in putting together justification for the implementation of various policy initiatives. The Commission itself, in its Issues Paper, says: "does this (government policies) adequately reflect the attitudes of all governments to smoking, or is it more complex than this?"

It is generally accepted that good public policy depends on (i) compelling, convincing evidence of the highest quality, and (ii) rational, clear and coherent use of that evidence to make public policy decisions.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

In the instance of *"prohibitions of smoking in certain locations"* and *"segregation of smokers from non-smokers"*, Philip Morris submits that there is a lack of compelling, convincing scientific evidence to support initiatives by Australian governments, whether it be to protect non-smokers from *"an environmental carcinogen"* or to *"discourage people from smoking"*.

Available scientific evidence does not persuasively support such policies if (as it appears) these policies are based on an alleged risk of chronic disease related to ETS exposure. In the absence of such support, Philip Morris suggests to the Commission that it is impossible to make coherent public policy decisions of the sort currently under consideration.

As noted in the Commission's Issues Paper, the government's justification for imposing, or suggesting smoking bans or restrictions, is based upon the contention that it is a proven *"environmental carcinogen"*.

World-wide data, including eminent scientific/medical evidence, fails to prove that environmental tobacco smoke/ETS or so-called *"passive smoking"* causes cancer, heart disease or other chronic diseases sometimes attributed to ETS exposure. Much of the evidence supports the proposition that ETS is not even statistically associated with these diseases:

- To date, 34 published studies have examined whether being married to a smoker increases one's risk for lung cancer. 28 of these 34 (i.e. 83%) report no statistically significant increased risk or a decreased risk of lung cancer.

- 14 studies have examined whether workplace ETS exposure increases one's risk for lung cancer. 12 of these 13 report no statistically significant association.

- 4 studies have examined ETS exposure in social settings, which report 8 different risk estimates for lung cancer. 7 of these estimates report no statistical significant association. The other reports a significant decreased risk of lung cancer.

A distinct minority of studies examining ETS/lung cancer (less than 15%) is portrayed as demonstrating that there is an increased risk of lung cancer "between 35 and 53%. By precisely the same reasoning, it can be said that other studies demonstrate that keeping pet birds increases the risk of lung cancer by 570%, that high dietary saturated fat increases the risk by 500%, cooking with peanut or grapeseed oil

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Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

increases the risk by 170% and frequent consumption of whole milk increases the risk by 100%. Yes, statistically studies support each of these propositions, yet no-one is calling for a ban on whole milk or pet birds.

The extreme weakness of the arguments supporting the claims that passive smoking is a significant contributor to chronic health diseases, has been noted by eminent scientific and medical commentators.

With regard to lung cancer, Peter Lee's (need ref. to who he is and appendix note) text entitled *"Environmental Tobacco Smoke & Mortality"* (1992) reviewed the studies pertaining to the topic and concluded:

> *"Considered in its entirety, the epidemiological evidence does not convincingly demonstrate that exposure to ETS increases risk of lung cancer among non-smokers".*

Earlier this year, Dr Armitage (ref. to who he is and appendix note) published an article in the Journal of Smoking-Related Disease entitled *"Environmental Tobacco Smoke and Coronary Heart Disease (1993)"*, in which he concluded:

> *"The case for ETS exposure causing CHD (coronary heart disease) is wholly unconvincing because almost all of the accepted 'causational' criteria remain unsatisfied. In the meantime, it is wrong that an ETS/CHD health scare has been blown up out of all proportion in the last few years by a passionate anti-ETS health lobby. Interpretative opinions are not proven facts; they must be challenged and a more balanced point of view presented to the general public."*

In Canberra, ACT Health has proposed (1993) government-mandated smoking restrictions, despite the fact that, in the highest levels of science, there is disagreement as to whether exposure to ETS causes disease in non-smokers.

Indeed, even the "authoritative" opinion relied upon by ACT Health for the proposition that ETS is dangerous in public places, and should be restricted or banned, are of dubious authority and weight for such proposition.

Three noteworthy examples of so-called *"authoritative opinion"* used by ACT Health to support their proposals for restrictions, are:

1. National Health & Medical Research Council Report on Passive Smoking (1986)

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

The NH&MRC stated in 1986 that it *"acknowledges that further research is necessary to confirm and elaborate these effects of passive smoking on health."* (page 45 of report, appendix...). The *"effects"* referred to are the *"inferences"* that NH&MRC was willing to draw on equivocal and inconclusive evidence.

As the NH&MRC is currently reviewing its 1986 research, it would be most prudent for ACT Health to await the outcome of that review before further actions to attempt to bring in mandated smoking restrictions.

2. International Agency for Research on Cancer

It has been claimed (by whom?????) that the IARC listed *"tobacco smoke"* as a group 1 carcinogen, and that smoking should be banned in workplaces as a result. However, a careful review of the 1986 monograph published by the IARC makes it clear that this body was making reference to *active* smoking, not ETS or passive smoking.

We would suggest to the Commission, that for ACT Health, or any other body, to rely on the IARC paper to support public policy in relation to smoking restrictions to overcome alleged ETS or passive smoking problems, is patently wrong and should be ignored.

3. United States Environmental Protection Agency Risk Assessment on ETS (appendix ....) released.....1993?

The risk assessment made by the EPA has been criticised by many eminent scientists, who have noted for example that the EPA based its risk assessment of lung cancer on only 11 of the 13 U.S. epidemiological studies available.

The two studies excluded were those by Stockwell(9) and Brownson(10). The EPA chose to exclude these studies because they were published after the arbitrary cut-off date earlier in 1992. It is noteworthy that the Brownson study is the largest study published on spousal smoking status and lung cancer in the U.S. and was sponsored by the National Cancer Institute. It reported no increased risk for overall exposure to spousal smoking.

When the results of these studies are added to the EPA's meta-analysis, the combined result is not statistically significant at the

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Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

accepted 95% confidence level, or for that matter on the less rigorous 90% standard applied by EPA.

Alvan Feinstein, Professor of Medicine and Epidemiology at Yale Medical School wrote recently (appendix reference???) in Toxicological Pathology that the EPA study on ETS *"simply ignored the inconvenient results and emphasised those that are helpful."* Professor Feinstein observed that government agencies funding scientific research often become *"mechanisms of advocacy."*

Further significant criticisms made of the EPA risk assessment are detailed in the attached paper "Smoke and Mirrors" : The EPA's Flawed Study of Environmental Tobacco Smoke and Lung Cancer" Huber et al, 1993 (attachment ??). Among their criticisms, Huber et al noted:

> *"In its report on ETS, the EPA did not comply with accepted principles of toxicology, chemistry, and epidemiology, nor with its own guidelines for undertaking cancer risk assessment".*

So little respected is the EPA Risk Assessment that the United States Occupational Safety and Health Administration has commissioned its own review of ETS to determine whether smoking in the workplace ought to be restricted. That is, it has specifically determined not to rely on the EPA report. This may be due to the congressional investigations of EPA practices, and the EPA's lack of scientific method and objectivity as widely reported in the press.

It is entirely inappropriate for ACT Health to have relied (even in part) on the US EPA risk assessment to provide credible support for its proposed smoking restrictions. As other authorities in the US have questioned the validity, or not relied upon, the EPA report, so, too, should the Commission and other Australian authorities not rely on it. In the absence of such support, it is impossible to make coherent public policy decisions of the sort currently under consideration.

The fact is the phrase *"passive smoking"* is misleading. It suggests that a non-smoker is exposed to the same thing as a smoker. This simply is not the case.(1,2) Environmental Tobacco Smoke (ETS) is very different from the smoke a smoker inhales. It is a hundred times more dilute and it undergoes extensive chemical and physical changes before it

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

reaches non-smokers.(3) To compare ETS with a smoker's smoke is like comparing apples and oranges.

In addition, virtually all of the substances known to be present in ETS are present in the air from other sources (such as office equipment, building materials, cleaning solvents and furnishings). Scientific studies indicated that non-ETS sources release the majority of these substances into indoor air.(3,4,5,6)

Because ETS is visible and easy to identify, it is frequently blamed for poor indoor air quality. However, scientific studies have concluded that inadequate ventilation is most often the real culprit. If these is a build up of smoke in the air, which indicates poor ventilation, then there is also a build up of other substances from non-smoking related sources.

Many studies from around the world report that ETS is typically a minor contributor to poor indoor air quality. For example, both US government and private studies on "Sick Building Syndrome" have reported that ETS is a direct factor in only 2-5% of the complaints in building investigated.(4,5,7,8) In contrast, more than half of the complaints in buildings investigated were traced to inadequate ventilation.

Indeed, scientists have had a major problem in measuring ETS in real-world settings because most chemical components of ETS are also produced by many other sources unconnected with smoking and also because many of the chemical components in ETS are present in such minute quantities that they are difficult to detect.3

Nonetheless, nicotine in the air is often used as a marker for non-smoker exposure to ETS. Results are sometimes presented in terms of "cigarette equivalents" as a means of illustration. The following are results of several studies in different locations:

Workplaces: It has been estimated that, in a workplace permitting smoking, it would take between 260 and 1,000 hours for a non-smoking worker to be exposed to the nicotine equivalent of a single cigarette.7,8,9 In other words, that worker would be exposed to between 2 and 7 cigarette equivalents during the course of an entire work year.10

Aeroplanes: Data from another study indicate that a person would have to take 11 round trips between New York and Tokyo (about 250 hours) in the non-smoking section of a

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Boeing 747 airliner before being exposed to the nicotine equivalent of one cigarette.[11] In some cases, the level of ETS in non-smoking section of aeroplanes is below the detection limits of even the most sophisticated monitoring equipment.[12,13]

Restaurants: A recent study indicates that it would take 300 hours of dining in a restaurant permitting smoking to be exposed to the nicotine equivalent of one cigarette.[8]

Taverns/Bars: Research out of Harvard University reports that one would have to spend 100 hours in a smoky bar environment to be exposed to the nicotine equivalent of one cigarette.[14]

Other scientific and technical research has demonstrated that proper ventilation, when adequately maintained, can drastically reduce the minuscule exposure levels referred to above.[6,15,16]

Smokers and non-smokers alike are entitled to adequately indoor quality through proper ventilation and filtration. Banning smoking may remove the indicator, but not the cause, of indoor air problems and Philip Morris rejected the illusory *"quick fix"* of banning smoking to solve indoor air problems. Nevertheless, some people find ETS annoying, which is why we encourage smokers to smoke with courtesy and common sense. We firmly believe that in any environment, both smokers and non-smokers can and should be accommodated.

Debate on passive smoking/ETS will clearly continue. However, Philip Morris believes it is important for those concerned with the issue, including governments and their instrumentalities, to give proper consideration to the arguments, put forward by many authoritative sources in Australia and internationally, about indoor air quality and ventilation as a key factor for focus when considering the passive smoking/ETS issue.

For instance, in the case of ACT Health, if the government truly believes that ETS poses some health risk, it is hard to understand why the issues of ventilation and segregation have not been thoroughly canvassed to address the claimed "problem". These are clearly less restrictive alternatives that may entirely alleviate the problem, to the extent that one exists.

Philip Morris brings to the Commission's attention, a technical analysis of the relationship between indoor air quality and proper ventilation undertaken by BESCA(????) engineers and

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Health Buildings International (HBI), where they propose that proper ventilation can entirely address the ETS issue, without resorting to severe restrictions or total bans.

BESCA and HBI's findings include the view that ETS was a contributor to poor indoor quality in only a small minority of buildings and, even in those, it was a small factor.

They also found that existing ventilation and filtration systems, if properly maintained, are also invariably sufficient to provide accommodation for both smokers and non-smokers; separate ventilation is not necessary to provide adequate indoor air quality for non-smoking and smoking areas; and, the rush to institute smoking restrictions or bans *"misunderstand or ignores scientific, technological and medical information available concerning interaction between ventilation/filtration and ETS."*

In more general terms, the late Dr Allan Crawford (need to ref to who he is etc???) questioned, in his paper, whether ETS exposure posed any health risks sufficient to warrant governmental imposition of smoking restrictions. In his paper, entitled *"Environmental Tobacco Smoke in the Workplace"* (appendix note), he concluded:

> *"From a scientific standpoint, the rush to promulgate workplace smoking restrictions is astonishing when one considers what the existing research shows"* (page 127 Dr Crawford's paper), and
>
> *"Government officials reviewing workplace smoking restriction proposals should beware the limited and inconclusive nature of the data concerning the asserted long-term health consequences of exposure to ETS in the workplace, and the growing body of data indicating that actual exposure levels are minute"* (page 131 Dr Crawford's paper).

With regard to the question of whether ETS causes health risks in public places, we draw the Commissions' attention to the most recent legal case concerning *"passive smoking"* in a public place, the Burswood Resort Casino (WA) case, which should cause government bodies to question whether smoking bans or restrictions can legitimately be justified on public health grounds.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

It is significant, in the Burswood case, that the Department of Occupational Health, Safety & Welfare was unsuccessful in its prosecution of the Burswood Casino, despite the fact that there were found to be moderate levels of ETS present i the casino.

The department alleged that casino employees were at a health risk from respiratory illness, impairment or reduced lung function due to ETS exposure.

In dismissing the claim against the casino, the court stated"

> *"Whilst ETS is annoying, and of discomfort to non-smokers, it has not been proved at the required standard, or at all, in this prosecution, that it is a risk to the health of the employees at the casino."*
> (Reasons for Judgement, page 9, 1993).

Philip Morris is in full agreement with an industry view that the less restrictive alternatives of ventilation and segregation must be carefully considered before legislation imposing smoking restrictions/bans can be justified, if at all.

At the scientific and medical level, there is considerable evidence, here in Australia and internationally, of the importance of good quality air in reducing or eliminating contaminants of any type inside buildings and the relationship of this to the issue of passive smoking/ETS.

Philip Morris urges the Commission to review the substantial writings on the issue in the context of considering policies on passive smoking/ETS and government actions in this area. Some of these writings have been submitted to the NH&MRC by HBI and BESCA through the Tobacco Institute of Australia.

10·2 Prohibitions on Sale of Tobacco to Minors

Philip Morris' position on the sale of tobacco to minors, and policy on juvenile smoking, is clear and unequivocal, as it has been for many years:

We do not believe that children should smoke or have access to tobacco products. We market our cigarettes only to informed adults who are entitled to make the decision to smoke.

Here in Australia, and in other countries, we have put money, time and effort into campaigns to help prevent minors purchasing tobacco products and to seek to reduce the incidence of juvenile smoking.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

In the 1987 Industry Assistance Commission inquiry into the tobacco industry, we outlined our activities, including the placing of signs in Australia's 40,000 retail outlets clearly stating that it was an offence to sell cigarettes to any person under the legal purchasing age. That distribution of signage was backed up by our salesforce to inform retailers of their obligations and Philip Morris determination to see action against the continuing sale of tobacco products to minors.

Again, in 1993, Philip Morris initiated a further program aimed at reducing the level of sales of cigarettes to minors at retail outlets.

This national campaign, designed to reinforce the legal prohibitions upon the purchase of cigarettes by young people, again took in all of the 40,000 retailers who sell tobacco products. Brochures and signage have been distributed, and are now displayed in retail outlets under the umbrella message *"It's the Law"*.(see appendix) The Philip Morris salesforce has reinforced the campaign objectives with retailers and continue to encourage retailer compliance with the law.

Although the company has undertaken these extensive retailer campaigns, it is not the company's role to act as a policeman in helping to stamp out sales to minors. We see our task as ensuring retailers, and the youngsters who seek to purchase tobacco products, know that it is against the law if the individual is under the legal purchasing age.

Even though the further task of prosecution is for police and other authorities, we strongly support strict laws that keep cigarettes out of the hands of young people and penalties for retailers who knowingly break the law.

In relation to the age limit, Philip Morris has campaigned with State governments, particularly those with a legal minimum age of 16 years, to establish a uniform national, minimum age of 18 years.

Philip Morris acknowledges that limiting access to the purchase of cigarettes is only one step in a number of initiatives that need to be undertaken to discourage smoking by young people.

We are, therefore, currently developing a broader campaign, focused upon initiatives for education and training to counteract peer pressure motivation, and similar factors which we believe are a major contributors to the problem of underage smoking, a fact supported by research in Australia and internationally. (insert reference)

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

The company is serious in its intent, and actions, in working itself, and with relevant authorities, to discourage smoking by Australia's young people. Equally, we re-state our view that adults, properly informed as they are on health issues, should have the right to make their own decision on smoking.

10.3 Publicly Funded Anti-Smoking Campaigns

There have been published several independently commissioned reports and assessments of the work of some of the publicly-funded anti-smoking organisations, including the various State health promotion foundations.

In one report, *"A Considerable Success"*: An Economic Evaluation of the Victorian Health Promotion Foundation by Professor Neville Norman (1992, appendix....????), commissioned by VHPF itself, a cost-benefit analysis of the Vic. Health is made, and broadly concludes:

- After five years of operation (1987-1992), the VHPF has been a considerable success
- On an extremely conservative estimate, the $121 million investment has returned more than $200 million in 1990 values and prices from the Quit campaign alone

The Norman report then goes on to broadly recommend:

- That the economic return justifies both the maintenance of the hypothecation system and substantial increases in the tobacco levy
- That a significant share of this increase be accorded to the VHPF
- That the *'efficiency'* notion be used more extensively in evaluating the use of funds for major recipients

In October, 1993, a report, *"A Question of Balance"* by the Price Waterhouse Economic Studies and Strategies Unit, commissioned by Philip Morris to evaluate the Norman Report, concluded that:

- The underlying analysis (by Norman) of mortality rates, benefits and application of a discount rate cannot support the conclusion that the Victorian Health Promotion Foundation (VHPF) is a success; and

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

- As no comparison is made against other potential uses of the funds applied to the VHPF, and no data is supplied on the internal efficiency or otherwise of the VHPF, an argument for an increase in funding for the VHPF cannot be sustained. Hypothecation itself is in direct opposition to this type of comparative analysis.

Further, in a broader review of the funding and operations of all health promotion foundations in Australia, commissioned by the Tobacco Institute of Australia, Price Waterhouse (October 1991, appendix..???) considered, among other issues, equity issues in funding the foundations, the cost to the community of health promotion foundations, the efficiency of the foundations, their effectiveness in meeting their objectives and their accountability.

The Price Waterhouse review was extensive and independent in its assessment of the health promotion foundations, and Philip Morris commends it to the Commission as an important, balanced contribution to the study of the tobacco industry in the context of the Commission's question on publicly funded anti-smoking campaigns.

10.4 Labelling Requirements for Specific Health Warnings

The Commission notes that Federal and State Governments, through the MCDS, have agreed on the need for clearer, stronger warnings to discourage people from smoking, especially to stop children taking it up.

Philip Morris has made it clear to federal and state governments that it believes there is neither data, nor logic, to support labelling recommended by the MCDS.

As we pointed out in correspondence to State and Federal Ministers and authorities, the MCDS proposal to appropriate more than 50% of the cigarette package is based upon the assumptions that young people (1) do not know of the reported health risks of smoking and (2) modified warnings covering most of the package will somehow stop youth smoking.

Recent Australian research shows these arguments are insupportable.

It is uniformly recognised that peer pressure, not lack of knowledge or awareness, is the primary influence on youth smoking and that generally there is universal awareness in Australia on the reported adverse affects of smoking on health.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

A study in 1993 by ANOP Research Services Pty Ltd supports this contention, showing that of adults (20 years and over) surveyed, 96% were aware of reported health risks and 100% of young people (15-19 years) were aware. The study surveyed 2,062 geographically representative Australians and 99.7% of all respondents nominated health risks associated with smoking in response to a series of three open-ended questions. A copy of the ANOP survey is appended.

In the public policy debate on the proposed new labelling and health warnings, policies has played an increasing part, with the debate emanating from an April 1992 MCDS decision to introduce new State based regulations requiring new and strong warnings. This included a requirement that the entire back of cigarette packets be taken up with prescribed warnings.

At the time of the July 1993 MCDS Western Australia was the only State to house gazetted regulations, and these had already been amended significantly.

On September 28, 1993, Victorian Government gazetted labelling regulations, consistent with European standards and requiring stronger and larger warnings. The following day the Federal Health Minister announced he would use Trade Practices Regulations to override the new Victorian regulations and achieve national uniformity, and then, in December, the ACT Government enacted labelling legislation consistent with the MCDS proposal but different from Victorian Regulations Also in December 1993, the WA Government gazetted new regulations which are gazetted differently from those previously gazetted and amended, consistent with the MCDS proposal, but different in some aspects from the ACT legislation and of course different from the Victorian Regulations.

At the end of January 1994, manufacturers are faced with a serious dilemma: how to manufacture for a single national market within which 3 different sets of regulations come into effect on different dates and may be overridden in the foreseeable future by a fourth set of regulations, different again from those currently in place.

The minimum implementation period required by manufacturers to comply with Government mandated labelling requirements is 12 months. This time-frame has been explained in great detail to Governments, but its significance for industry has been largely ignored.

The Victorian Regulations provided a 12 month implementation period, ACT 4 months and WA 6 months. Government officials have argued that manufacturers have known for over 12 months that new

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Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

labelling will be required and therefore should be in a position to implement new regulations less than 12 months after their gazette. However, it is unreasonable to expect compliance with any proposals until they become law, or unless there has been mutual agreement that the proposed are reasonably necessarily and the time-frame practically achievable.

If regulations are to continue to be effective in controlling certain practices across a whole range of business activities, then manufacturers cannot be expected and certainly should not be obliged to make expensive business decisions on what they think the regulations might require. Such decisions can only be made in a climate of certainty. It is unacceptable for a business alleged to be in breach of regulation to plead ignorance of them.

Similarly, it would be financially irresponsible of businesses to spend money on changing manufacturing processes on the basis of regulatory changes foreshadowed in ministerial press releases.

10.5 Prohibitions on Advertising

"There is little evidence that advertising results in additional smoking, as with many products, cigarette advertising mainly shifts consumers among brands". U.S. President's Council of Economic Advisors. (1)

The contention that tobacco advertising influences people to smoke overlooks the function of advertising in a "mature" product market; such as the market for cigarettes, toothpaste, laundry detergent or cars.

In a "mature" market, where the product category is long established and awareness of the product is universal, advertising does not generally operate to increase overall demand. Advertising instead, operates to maintain or expand market share within the product category..... to maintain the loyalty of consumers who already use the brand being advertised and to switch consumers who use other brands. Cigarettes are a long established product and awareness of cigarettes is in fact so wide spread that they are the very model of a "mature" product category.

The aim and effect of advertising for such "mature" product categories is to promote, and to provide information on, particular brands of the product, not to promote the product category itself. Many studies have found that advertising in such markets is not significantly related to aggregate product demand. (2)

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Thus, denying product information to consumers (which effectively limits competition) will not effect broad consumer demand patterns. Government policies which aim to reduce smoking prevalence by instituting advertising bans are therefore extremely unlikely to have any impact. (3).

The fact is that, in "mature" markets, advertising and consumption are unrelated, thus there is no relation between smoking incidence - in juveniles or adults - and advertising restrictions. Indeed, numerous studies indicate that consumption is declining in many countries where advertising is allowed, while increasing in countries where it is prohibited. (3,4,5,6,7)

For example, in Finland, where tobacco product advertising has been banned since 1978, a 1991 study published in the Finnish Medical Gazette (16) reported that smoking increased in Finland until 1976, two years before tobacco product advertising was banned. Then,

> *"The consumption of tobacco products and smoking among young people started to fall. However, in the mid 1980's the figures once more started to rise, and on the basis of the situation of the early 1990's, smoking does not appear to be decreasing at the moment".*

Tobacco product advertising has been banned in Norway since 1975, yet a study by Gotestam etal published in the Journal of Norwegian Medical Association, 1990 (8), reported that "*The total incidence of daily smoking among Norwegian adults (defined as persons 15 years of age and older) remained essentially unchanged between 1979 (38%) and 1989 (36%).*" (8)

In 1992 when further assessing the hypothesis that an advertising ban leads to reduced tobacco sale and to reduced smoking in Norway, Gotestam etal concluded, *"The results supported neither hypothesis"*, and that "*The enacted legislation does not seem to have affected either tobacco sale or the number of regular smokers in Norway*". (17)

Consistent with this conclusion, a team of anti-tobaccco researchers told the 7th World Conference on Tobacco and Health in 1991:(10)

"Although Norway, in many respects, has been a pioneer in the campaign against tobacco, the prevalence of smoking in Norway has changed very little in the past eight years. The prevalence of daily smoking among men was reduced from 52% in 1973-1974 to 40% in 1981. This percentage has remained nearly constant since then. Among women, the prevalence rate of regular smoking has been

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

constant, about 32 - 33% since 1973 "During the period when the prevalence of regular smoking was constant in Norway, the prevalence of regular smoking in the USA was reduced by between 1/3 and 1/4".

Major cross country studies disclose similar findings. A 16 - country study of eight Soviet Bloc and eight Free-Market countries (18) disclosed that smoking increased.... sharply in some cases.... between 1970 and 1984 in the Soviet Bloc countries, even though advertising did not exist during this period.

In the eight Free-Market countries, included in the study, consumption was not substantially affected by tobacco product advertising bans or strict controls. In Italy for example, where advertising was banned in 1962, adult per capita consumption increased from a base of 100 in 1960 to 182 in 1984, and in Iceland where advertising was banned in 1971, per capita consumption increased from a base of 100 in 1971 to 113 in 1984. (18)

In Eastern European countries, data from the World Health Organisation (19) indicate that sales of cigarettes rose between 4 and 22 per cent from 1975 to 1989 even though cigarette advertising was not allowed.

As with adult smoking incidence, surveys on smoking trends among young people in countries where cigarette advertising has been banned or severely restricted, have found that these decisions have been ineffective in reducing smoking among their young people. (8,9,10). If advertising were a significant influence on smoking among juveniles, one would expect juvenile smoking to be higher where tobacco advertising is permitted than where it is not. But a WHO survey (11) found *"no systematic differences"* between juvenile smoking in countries where tobacco advertising is banned and in those countries where it is not. Indeed the WHO survey and three Children's Research UNIT studies (12) disclose that the incidence of smoking among young people is higher in many countries where advertising is banned than where is not.

Those in favour of banning or restricting tobacco product advertising assert that such advertising not only influences adult smokers to continue smoking, but that it also causes children and teenagers to decide to smoke. In fact, available evidence indicates that advertising is among the least influential factors involved.

In an update focusing on the prevalence of youth smoking among school children in 1986-1987, Aaro and two colleagues reaffirmed the results of an earlier study. (25). They found, in general, that the

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

countries with the highest incidence of youth smoking are those in which tobacco advertising is banned, while the countries with the lowest incidence of youth smoking are those in which some tobacco advertising is permitted.

In both Finland and Norway, where tobacco advertising has been banned for more than a decade, Aaro and his colleagues found that in Finland 29 percent of the 15-16 year old boys and 20 percent of the 15-16 year old girls were daily smokers in 1986-1987; while in Norway 16 percent of the 15-16 year old boys and 17 percent of the 15-16 year old girls were daily smokers in 1986-1987.

In both Austria and Switzerland, by contrast, tobacco advertising is permitted, Aaro et al noted that:

> *"In Austria 12 percent of the 15-16 year old boys and 13 percent of the 15-16 year old girls were daily smokers in 1986-87, and in Switzerland 10 percent of the 15-16 year old boys and 12 percent of the 15-16 year old girls were daily smokers in 1986-1987.*

Significantly, in Hong Kong a government sponsored study (27), no children mentioned advertising as a reason for smoking. The Hong Kong study confirms that parents and peer group appear to be the most significant influences on youth smoking.

In Singapore, where tobacco product advertising has been banned since 1970, the Health Ministry claims that smoking among 15-19 year old boys jumped from 5.5. percent in 1987 to 12.3 percent in 1991, and that smoking among 15-19 years old girls increased during the same period from 0.1 percent to 0.7 percent. (28)

A "Special Report on the Impact of Tobacco Advertising" published in the International Journal of Advertising in 1990 (26) reiterates these conclusions:

> *"Cross-national studies on smoking indicate that the prevalence of smoking is high in countries with an almost complete ban on tobacco advertising (Australia, Canada, Norway and Sweden) and low in countries with a more liberal advertising climate (Argentina, Hong Kong, Japan, Kenya, and the Philippines). This indicates that any reinforcing and justifying effect of advertising does not cause adolescents to start smoking".*

So far as young people are concerned, the most forceful determinants of smoking are parents, peers and older siblings (13,14,15), and

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

before launching their attack on cigarette advertising, anti-smoking advocates and government researchers appeared to acknowledge that these factors are the primary influences on smoking by young people.

- In 1983, Dr. Mortimer Lipsett, the Director of the US National Insitute of Child Health and Human Development, testified that *"The most forceful determinants of smoking (by young people) are parents, peers, and older siblings"*. (20) Dr. Lipsett also noted:

- *"If one parent smokes, the child is twice as likely to smoke as one reared in a non smoking household. If both parents or one parent and an older sibling smoke, the chances become four to one. If the child's best friend smokes, there is a 90 percent probability that the child will smoke too". (21)*

Researchers looking at the long-term correlation of factors provide further support for the thesis that peers are the most dominant influence in youth smoking. (22) These findings reflect a world-wide phenomenon and are not limited to the United States.

- The Swedish National Smoking and Health Association concluded in 1983 that *"the smoking habits of young people are dependent on the smoking habits of their parents"*. (23)

- Monique Begin, then Canada's Minister of National Health and Welfare, stressed in a 1983 address that *"The people who most influence a child to start smoking are his or her friends and family"*. (24)

The decisive influence of family and peers on youth smoking is again supported by a four-country survey conducted in 1983-84 by the World Health Organisation (WHO), the results of which were published in 1986: (11)

> *"When young people start smoking, the most important predictor is the smoking behaviour and smoking related activities of significant others".*

The WHO survey further reported that *"The strongest statistical relationships are found with the smoking habits of the best friend"*. The survey also found that smoking among school children is *"strongly related to the number of smokers in the family"*, and found *"no systematic differences"* between the smoking behaviour of young people in countries where tobacco advertising is completely banned and in countries where it is not.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

Particularly instructive is the testimony in 1986 before the House Subcommittee on Health and the Environment by Dr. Roger D. Blackwell, Professor of Marketing at Ohio State University, and Dr. Scott Ward, Professor of Marketing at The Wharton School, University of Pennsylvania. (29) Dr. Blackwell explained that:

> *"From his parents a child acquires basic attitudes toward smoking. The more the parents smoke, the more likely the child will smoke; the more the parents discourage smoking the less likely the child will smoke".*
>
> *"Friends also play a significant role in the youngster's decision to try smoking and become a smoker. And so does the image of the smoker that most children develop. Children report a distinct image of the stereotypical smoker, and it is not the flattering image that anti-tobacco advocates attribute to cigarette advertising".*
>
> *"The stereotypical smoker is viewed by children as less educationally successful, less healthy, and 'tougher' than the stereotypical non-smoker, and non-smokers generally view other non smokers as more desirable to have as friends than smokers".*
>
> *"None of the research suggests that advertising influences children to view smoking in a positive light, we are talking about not intent but actual response among the children. To the contrary, the research that is available revealed in young people a scepticism and distaste for cigarette advertising".*

Given the demonstrated role that parents and other role models play in smoking by young people and the absence of evidence that advertising has any significant effect in this regard, there is no reason to believe that banning cigarette advertising would lead to reduced smoking among young people.

Clearly, three factors flow from these various studies, (a) there is not evidence to support the view that a ban on advertising would have a positive effect on smoking habits, (b) no empirical research has been able to show that tobacco products advertising leads to greater tobacco consumption, and (c) there is no evidence to suggest that advertising entices non-smokers, particularly young people, into becoming smokers.

Philip Morris believes therefore that its opinion that advertising does not promote the uptake of smoking is fully supported. Thus the

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

virtually total bans applying in Australia to the advertising of tobacco products, are both unsupportable and unreasonable constraints on the company's ability to communicate with smokers; and impose unnecessary commercial constraints on the company's ability to market its products in an intensely competitive market. Products which are, in fact, legal to produce and consume.

The same holds true for bans imposed on tobacco company sponsorship which do not in fact constitute advertisements.

11. Current Assistance to Growing and Manufacturing/Removing Impediments and Economy-Wide Efficiency

The Commission is to quantify the extent of any assistance provided to the industries and consider recommendations which will be directed at determining appropriate tariff assistance to put in place following cessation of existing arrangements for the industries, along with identifying ways of making the industries and the economy more efficient.

Participants may wish to comment on what they consider to be appropriate tariffs to apply to tobacco leaf and products, and give reasons for their choice. Should rates equal the average tariff rate. If not, why not?; should tariffs for leaf and tobacco products be set at the same level?

11.1 Eliminate Tariffs

There is no need for a continuation of tariff assistance for the tobacco industry . Without tariffs, we expect that:

1. Industry efficiency will be encouraged.

2. Improved efficiency will ensure the industry is more competitive.

3. Consumers will benefit and export opportunities will be enhanced.

4. Export growth will generate increased employment with flow-on benefits to local industries.

5. There will be no need to maintain bonded warehouses for tobacco leaf or the duty drawback system (currently essential for maintaining the competitive position of manufactured product exports). Associated costs and administrative systems for HM Customs and industry will be eliminated.

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

6. There will be no perpetuation of the inefficiencies seen under TISP with reduced focus on quality improvement, cost efficiency, productivity and market-driven selling systems.

7. Government policy will be satisfied.

11.2 Tariffs and Funding Assistance

If, however, tariffs are retained to assist industry adjustment during the early stages of deregulation, we strongly support the concept of the revenue from tariffs being used to fund tobacco industry activities, such as:

- Making grower premiums available
- Assistance (set aside payments) to growers who are unlikely to be viable in the long-term
- Funding the TRDC research programs
- Assisting and promoting export programs
- Improving the efficiency and cost base of the industry infrastructure (e.g. modern leaf processing plants)

This has been the approach used in the European Common Market.

If tariffs do remain after 1995, they should be phased out over a period of time, say 5 years.

Continuing tariff assistance should be based on a flat rate, or specific basis. The level of tariffs applied to imported manufactured products should maintain equity with the tariffs applied to imported tobacco, as local manufacturers, andultimately the local tobacco producing industry, will otherwise be disadvantaged.

11.3 Withdraw Tariffs/Developing Country Imports

Lower tariff rates applied to imports of tobacco and manufactured products from developing countries should be withdrawn.

The markets against which Australian domestic growers are competing are basically all developing countries. Assistance is not necessary on the higher quality and higher priced tobaccos, where the developing countries are fully able to compete, given their lower cost base.

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Australian growers will also benefit by this approach. They will receive assistance in the low quality/cost sector of their production, whilst leaving incentives to improve quality for the long-term viability and sustainability of the industry.

The rationale is also consistent for manufactured products, as production costs in developing countries are typically lower than those of developed countries, which are therefore less competitive.

12. GATT Implications

Philip Morris is concerned that the proposals emanating from the Department of Foreign Affairs and Trade on GATT tariffication will have the direct effect of negating Government policy to remove protection from the Australian tobacco industry.

We believe that the timings associated with the GATT proposals make no sense and are of no benefit, either to industry or Government.

As we understand it, the proposed date for implementation of the Uruguay Round is 1 January 1995, or by 1 July 1995 at the latest. Abolishment of the T.I.S.P. and the L.L.C.S. is scheduled for 30 September 1995 and we understand that the tariff rates to apply after this date are to be driven by the recommendations of the I.C. inquiry. It therefore appears that the rates and structure as proposed from the Uruguay Round would, at the most, apply for a period of 9 months (1 Jan 1995 to 30 Sept 1995), or possibly for as little as 3 months (1 July 1995 to 30 Sept 1995).

The GATT proposals also envisage a quota for imported tobacco, with a higher tariff rate being applied to imports in excess of this quota. We see no need for any such quota. As currently formatted, we believe the proposals are unworkable. In order to achieve equity amongst domestic manufacturers, we believe it would be necessary for this base quota to be allocated to manufacturers according to a formula, and we see considerable difficulty in determining the basis and mechanics for such a formula. In addition, it is proposed that the tariff rates for imports in excess of the quota of 11,184 tonnes per annum be at a level of 30%, declining to 25% over a period of six years. This rate is both totally excessive and unnecessary.

With the quota applying, there would be every incentive for manufacturers to fully utilise it. With projected total usage levels, the proportion of local tobaccos used would fall away dramatically, (see charts and tables, *Fig.* .....) to the extent that the critical mass for the Australian industry would not be met. A total collapse of the growing industry would occur.

Philip Morris believes that applying the quota component of the GATT proposals is contrary to interests of the domestic growing and manufacturing industries, and inconsistent with Government policy on assistance to Australian industry. In fact, we see no need to introduce any of the current GATT proposals. Instead, we

Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000

growers and manufacturers. This could be achieved through a commercial agreement with jurisdiction under civil law to cover the interim period between Jan 1995 and the already published date for termination of the L.L.C.S. This would allow the I.C. inquiry to zero base its recommendations, take account of Government policy and reflect the commercial conditions that impact the tobacco industry. Tariff levels and structures should be maintained as they now stand until 30 September 1995, with the industry operating after that date, and with tariff rates and structures as ultimately recommended by the I.C.. Alternatively, the L.L.C.S. will need to be terminated before 30 Sept 1995 at a time to coincide with the introduction of the GATT proposals.

We are concerned that the information emanating from D.F.A.T. makes no comment on imported manufactured products. We believe any tariff assistance applied to imported tobacco should also be reflected, on an equitable basis, in the tariff rates for imported manufactured products. We question whether there will be quotas associated with such imports, what structures and rates will apply, and how will any quota be distributed? If domestic manufacturers are disadvantaged this will impact the whole industry, the levels of employment, the balance of trade and the flow-on benefits into the local economy.

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Source: https://www.industrydocuments.ucsf.edu/docs/yxfk0000